Royalty-In-Kind

Under the Mineral Leasing Act of 1920 and the Outer Continental Shelf Lands Act of 1953, the Federal Government, as lessor, may take part or all of its oil and gas royalties "in kind." The Secretary of the Interior, exercising discretionary authority, has historically determined that certain oil refiners do not have access to a secure supply of crude. The Federal Government may direct Federal lessees to pay their royalty shares in crude oil, rather than "in value" as cash. The Federal Government then sells the royalty-in-kind (RIK) oil to eligible refiners at a price consistent with applicable laws and regulations. Contracts with the refiners are usually made for a period of 3 years.

Four onshore oil RIK contracts were in effect in 1996. Collective purchases by the onshore refiners fell 5 percent, from 2.4 million barrels in 1995 to 2.3 million barrels in 1996. The royalty value of the purchases rose, however, 11.2 percent, from $41.1 million in 1995 to $45.7 million in 1996 (table 36, and figures 42 and 43). Domestic oil prices are materially influenced by the international market. Low world inventories of oil and high demand in the United States, Europe, and developing nations in Asia caused oil prices to rise in 1996.

One Pacific and nine Gulf of Mexico offshore oil RIK contracts were in effect at the beginning of 1996. One Gulf refiner sold his refinery and terminated his contract during the course of the year. The offshore refiners collectively purchased 30.7 million barrels of RIK crude in 1996, up significantly over a corresponding figure of 19.3 million barrels in 1995. The royalty value of the purchases rose from $322 million in 1995 to $520.5 million in 1996 (table 36, and figures 42 and 43). The increase in royalty value is again due to higher prices resulting from low world inventories of oil and high international demand.

The increase in offshore RIK activity in 1995-96 reflects an effort by the Minerals Management Service to provide a secure supply of crude oil to refiners in the Pacific and Gulf areas.

Total RIK crude, with a royalty value of over $566.2 million, represented approximately 30 percent of the oil royalties paid to the Federal Government in 1996 (tables 3 and 36). The 1996 figure represents the highest RIK royalty value since 1984 when royalty value totaled $792.2 million.

Table 36. Summary of Royalty-in-kind oil taken as royalty payments for Federal mineral lease sales volume, Calendar Years 1976-96

	Federal Onshore		Federal Offshore		Total RIK Oil	
	Barrels Sold	Royalty Value	Barrels Sold	Royalty Value	Barrels Sold	Royalty Value
1976-86	87,985,357	$1,487,912,313	203,318,781	$3,549,896,466	291,304,138	$5,037,808,779
1987	4,920,903	82,960,764	820,206	10,780,495	5,741,109	93,740,259
1988	6,928,986	94,314,227	861,027	7,951,951	7,790,013	102,266,178
1989	6,021,694	95,241,410	820,300	9,295,589	6,841,994	104,536,999
1990	5,800,634	118,816,887	733,582	11,544,477	6,534,216	130,361,364
1991	4,799,004	95,816,902	674,113	9,050,729	5,473,117	104,867,631
1992	3,956,582	69,303,308	713,272	8,537,273	4,669,854	77,840,581
1993	3,130,328	51,719,709	505,386	5,965,712	3,635,714	57,685,421
1994	2,776,868	39,493,665	483,292	4,268,058	3,260,160	43,761,723
1995	2,419,542	41,125,635	19,305,519	321,988,629	21,725,061	363,114,264
1996	2,298,571	45,712,144	30,716,298	520,527,939	33,014,869	566,240,083
Total	130,938,459	$2,222,425,464	259,051,876	$4,459,806,929	389,990,335	$6,682,232,393

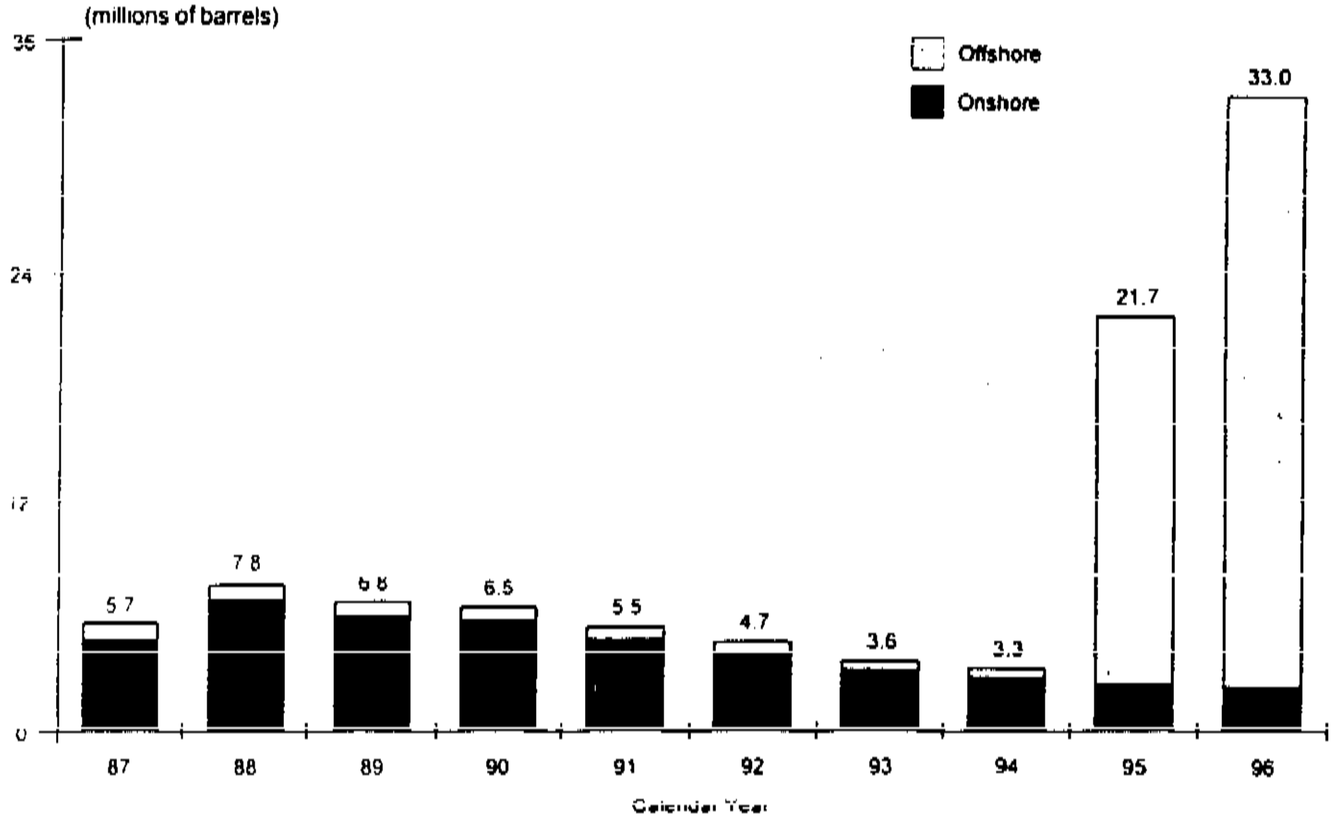

Figure 42. Royalty-in-kind barrels of oil sold by land category, 1987-96

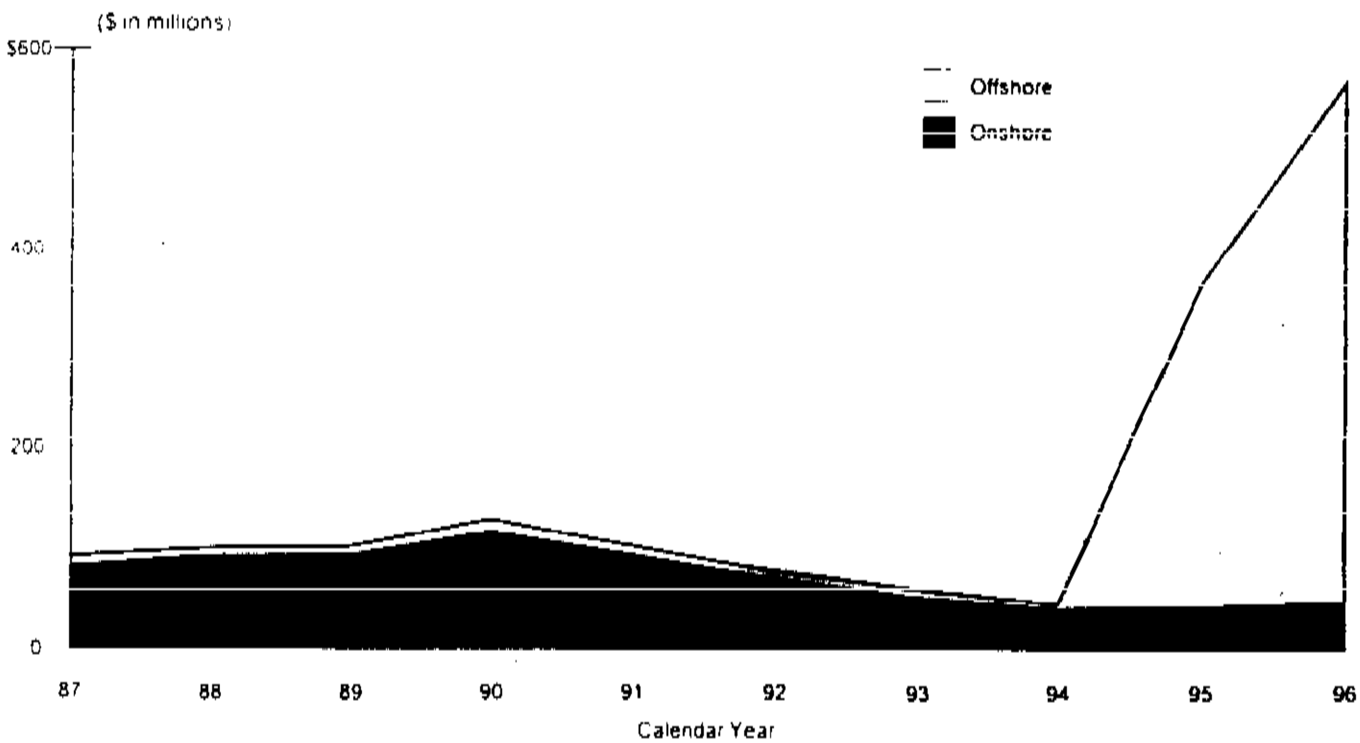

Figure 43. Royalty-in-kind oil royalty value by land category, 1987-96

Royalty-in-Kind -- Oil RIK Study

ISSUE: RIK program review including valuation and volume measurement

STATUS: Vern Ingraham and Jim McNamee briefed the Quality Council on September 12, 1997. The Associate Director for Royalty Management approved the recommendation to conduct a pilot to test certain volume and valuation scenarios.

A pilot team is being established and a pilot plan is being prepared. The lease selection process has started. A letter will be sent to the Associate Director for Offshore Minerals Management during the week of September 22, 1997, announcing this pilot and requesting participation of the GOM's Office of Production Development. Preliminary contacts have been made with this office. Refiners and operators are being contacted and requested to participate in the pilot. The pilot will include the production months of January through June 1998. Analysis of pilot findings will be completed in early November 1998.

In a separate but related effort - Phase II of the Oil RIK Study - certain additional issues are being reviewed. These include (1) development of a Determination of Need process which will detail and explain the process for making a determination of need for activation of an eligible refiner oil RIK contracting cycle and (2) the formula to be used in calculating the administrative fee.

BACKGROUND: In response to recommendations of the RPC Subcommittee on Royalty Reporting and Production Accounting, we initiated the Oil RIK Study in September 1996. The study team's first report was issued in September 1997. The second report will be issued in December 1997 covering certain RIK administrative issues. The third and final report will be issued in December 1998 addressing the pilot and will recommend implementation of a reengineered eligible refiner oil RIK program. The study team is comprised of 9 members from RMP, PMI, and STRAC (North Dakota and Wyoming).

CONTACT: Vern Ingraham (303) 231-3116